

# Navigating the Tax Maze: California Sales Tax Obligations for Nonprofits

07.08.15 | Linda J. Rosenthal, JD



*Two friends enter a deli in downtown San Diego for some take-out. One orders a ham and cheese sandwich and is charged \$5.95. The other orders the same, but her sandwich is toasted. She's charged \$6.43.*

Same food, same store – but the hot sandwich costs more than the cold one. That's an example of the inscrutable sales tax laws encountered by every Californian who has ever ordered food to go.

*"What does any of this have to do with us?" you say. "We're a tax-exempt organization!"*

Simple enough: Your 501(c)(3) tax exemption relief is from federal *income* tax only. If, as is likely, you have an exemption letter from the California Franchise Tax Board as well, that means only that you are exempt from state *income* taxes.

What about sales taxes? What about property taxes?

You may or may not qualify for exemptions under the entirely separate statutes that govern these additional taxes. For this post, we'll focus only on the California sales and use tax laws.

## *Sales Taxes: A Collage of Weird Exclusions*

Around the United States, many 501(c)(3) organizations have the benefit of broad exemptions from their states' sales tax laws.

California is different. "A charity that sells items may be required to collect and remit to the state sales tax on goods sold. In California, there is no general exemption from sales tax for charities. Rather, a variety of narrow exemptions apply to certain charitable activities."

The bottom line is that there is "no general sales and use tax exclusion for nonprofit organizations..." There is no sweeping provision that exempts sales

to or by nonprofit organizations.

You must assume, at the outset, that your organization will be liable the same as any other retail seller in the state to comply with the sales tax laws and registration requirements. Only certain – narrow – categories of charitable organizations, and certain types of activities, qualify for sales tax exemptions generally, or on selected sales but not on others.

And these laws may apply to transactions and interaction with donors and others that you would not ordinarily think of as traditional sales of goods subject to sales taxation. For example, when a charity has a gala fundraiser, the sales of items at the evening's silent auction are subject to sales tax, as are the delicious meals served to the donors.

Your task is to hunt down and identify possible exclusions and exceptions; no easy job. "It's complicated" – as the recent movie title suggests. More accurately – and to put it charitably – the California sales tax laws are mind-numbingly complex, confusing, and downright inexplicable.

Why is that? Each year, California rakes in tens of billions of dollars from sales and use taxes. Lawmakers are loathe to put these valuable revenue streams off-limits to the state coffers. Tax breaks are horse-traded behind closed doors with little rhyme or reason. Like sausage-making, the legislative process is unappetizing.

### *Defining the Tax Obligation*

We're all familiar with ordinary retail sales taxes: a percentage of the purchase price of personal property (on top of the purchase price) that the consumer pays, and the seller collects and turns over to the State Board of Equalization. Buying a dress at a department store, for example, is the type of classic "sale" that triggers a sales tax obligation.

Actually, the sales tax is a levy on retailers of tangible personal property for the "privilege of selling tangible personal property at retail in California." The retailer is authorized to collect the amount due from purchasers; as a result, the tax on retailers is effectively passed on to (i.e., "reimbursed" by) consumers.

Use taxes are related to sales taxes, but it's either one or the other that is imposed – not both. The use tax is imposed on all "retail purchases of personal property outside California for use, storage, or consumption within California" or otherwise on items purchased without payment of sales tax. For purposes of this post, we'll talk about "sales taxes" but note that the discussion applies equally to use tax.

### *Applicable Law*

The state statutes that apply and explain California's sales and use taxes are Revenue and Taxation Code Sections 6001. There are regulations as well,

along with rulings of the BOE Sales Tax Counsel. Occasionally, a disputed matter reaches the courts.

The Board of Equalization's website is a useful resource for understanding the sales tax laws. In particular, Publication 18: Tax Tips for Nonprofit Organizations is a valuable introduction and overview of the narrow exceptions for certain nonprofits and for specific transactions. Publication 61, Sales and Use Taxes: Exemptions and Exclusions lists all of the exclusions and exemptions, including and beyond those related to nonprofits, like the necessities of life exemption for certain food items.

There's also Publication 107, Do You Need a California Seller's Permit?

Whether or not an organization or certain of its sales are subject to sales tax, it may be required to obtain a seller's permit from the State Board of Equalization. See also Publication 73, Your California Seller's Permit.

#### *A Few Examples*

When you read Publication 18, you'll find out:

- Why sales of tickets at your events “that buyers will exchange for food, beverages, or other physical products” are subject to sales tax, but sales of “tickets for concerts, movies, plays, shows, and similar events when food and meals are not included in the ticket price” are exempt;
- Why “sales of tickets for game booths *where prizes are guaranteed* to each ticket purchaser, even when the prizes have little value” (e.g., “white elephant, fish pond, grab bag, and ‘pitch-’til-you-win’ games”) are taxable, while “sales of tickets for game booths and raffles *when prizes are not guaranteed* to every ticket purchaser” are exempt; and
- Why the Salvation Army's thrift shops are not subject to sales tax, but why thrift shops run by other nonprofits must collect and pay over the tax.

You'll also learn that:

- “Under certain circumstances, sales tax does not apply to sales by an authorized nonprofit museum auxiliary association ... that assists a California city or county museum.”
- “Sales or use tax does not apply to a veterans' organization's sale or purchase of ‘Buddy Poppies,’ and similar symbolic, temporary lapel pins when both of the following conditions are met: the pins are sold or purchased by the Veterans of Foreign Wars or other specified organizations ... and the pins memorialize U.S. military veterans killed in foreign wars”; and
- “Tax does not apply to sales of meals or individual food products to *school students* when the sales are made by . . . any blind person operating a restaurant, vending machine, or

vending stand at an educational institution” – but only if the meals are “served to students at a time regularly set aside for meals, not at recess or breaks.”

Getting the idea that “it’s complicated?” Ok. Now, back to that ham and cheese sandwich:

- If a nonprofit serves hot prepared food to go at a fundraising event, the sale is taxable, but if cold beverages to go are served at the same event, the sale is *not* taxable – except for alcoholic and carbonated beverages. But when cold beverages are served in a combination package, they may be taxable. And when a combination food package includes a carbonated beverage and one or more cold food items (for example: cold sandwich, chips, candy, and a soft drink), the tax applies only to the portion of the selling price that represents the charge for the carbonated beverage.

All clear?

### *Conclusion*

Don’t get caught in noncompliance problems with the State Board of Equalization. Learn about these taxes and determine which, if any, of your organization’s activities may be subject to sales or use tax. Determine if you need a seller’s permit (even if some or all of your activities are exempt from sales tax).